

THE PROBLEM OF INEQUALITY IN INCOME IN GEORGIA AND THE ROLE OF PROGRESSIVE TAXATION IN ITS ELIMINATION

George **ABUSELIDZE**
Batumi Shota Rustaveli State
University, Georgia
george.abuselidze@bsu.edu.ge

Jilda **ABASHIDZE**
Batumi Shota Rustaveli State
University, Georgia

Anna **SLOBODIANYK**
National University of Life
and Environmental Sciences
of Ukraine

Abstract: One of the most important factors for the development of the country is the functioning of the tax system; however, with the development of the functioning of the tax system is important, which ensures the economic well-being of the country to improve the welfare of the population. Along with taxes it is important to define the level of inequality between different layers of population. In this regard Georgia, as well as other developing countries, has an unfavorable situation and needs to take appropriate measures.

Reason of research: In order to eliminate the inequality of income, it is necessary to carry out such measures, which will improve the tax system of Georgia and will solve the problem of equality. In order to eliminate the inequality of income, we need to consider the possibilities of introduction of progressive taxes. It is noteworthy that the progressive taxation method of revenue contributes to the implementation of the social function of tax and equity distribution in comparison with the country's wealth.

Research object: One of the main sources of tax revenue is income tax and taxation of taxes in a progressive way. Also the right to introduce a taxable minimum.

Research Methodology: Conducting empirical analysis based on the data of the National Statistics Office of Georgia and Ministry of Finance of Georgia, Analyze studies conducted in this direction. The analysis of documents in fiscal policy was carried out during the research process. Surveys were conducted by means of qualitative and quantitative methods.

Keywords: Tax policy, income tax, tax burden, budget, well-being

Introduction

The level of community life is determined by different criteria and different indicators. The country's gross income may be high, but most of it is distributed to a small number of people. In this regard, a significant study was prepared by Italian statistician Corrado Jinn in 1912, it shows how well the income is distributed. The highest rate of Gini is recorded in Sweden - 0.25, the most equitable distribution is around the world, the highest is in Seychelles -0.658¹. This indicator in Georgia is 0.421 or 42.1%.

Duncan and Sabirianova (2016) find that progressivity reduces inequality in observed income, but has a significantly smaller impact on actual inequality approximated by consumption based Gini indices.

As we have seen, The Gin Index for Georgia is 0.42, which is quite high in equality and it is necessary to alleviate the situation with certain measures. Due to this, that amounts raised by income tax there is a large part of tax revenue. Our attention is concentrated directly income tax and Inequality associated with it. Labor remuneration is clearly different between different layers and therefore, the volume of taxes should be paid attention.

Literature Review

Tax as an important element of the system of economic relations is so complicated without alternatives in fiscal policy that it always becomes an actual issue in the public discussions (Abuselidze, 2015, p. 602). The study of the optimization of taxable income taxes in the modern stage is not only not only science but also an important concern for practitioners. First of all, the severity of this tax is based on the income tax analysis and impacts the welfare of society. Secondly, it is one of the major tax revenues for the budget, which is predictably predictable, which is more or less accurate and dependent on the functioning of the state to fund the necessary expenditures. It is universally recognized that tax burden affects not only budget revenues, but investments, production factors, price standards etc. Finally, all above affects socio-economic position of country (Abuselidze, 2013, p.1451).

¹ Human Development Reports, 2014.

Adam Smith regarded taxes as the index of freedom for tax payers, but for Montesquieu nothing and no one needs such a wisdom and mind as defining tax size and that part, which stays with a tax payer.

Smith wrote about the necessity of existing optimal tax policy in the country: “The owner of the capital is actually the citizen of the whole world and doesn’t represent the property of one country. He will immediately leave the country with undesirable tax condition and invest his capital in the country where he will be able to run his business and property without pressure” (Smith, 2011).

Adam Smith and David Ricardo (Ricardo, 1937) pointed to the factors determining real addressees of tax burden in their works. Adam Smith connected size of wages to elasticity of labour supply, but David Ricardo developed the ideas related to reaction of demand and supply regarding change of price for different goods, i.e. he considered elasticity of demand and supply a reference point. These considerations underlie the modern views which explain the problems of shifting of tax burden (Abuselidze, 2012, p. 497).

Unfortunately, most of the authors do not pay attention to the question of different tax regimes and rates influence on macroeconomic balance and employment level. However, we disagree with the Laffer-Keynes theory postulates, considering that introduction of optimal mean tax rates only is not able to increase employment level, initiate establishment of a new balance and mobilization of maximal tax revenue in the budget (Abuselidze, 2011, p. 163).

1. The role of tax system To improve the socio-economic situation of the country

1.1 Taxes and their importance in the process of revenue equalization

Taxes are mostly related to property ownership and with income. Therefore the size of the revenue is significantly determined tax base size. The state has a significant leverage in the process of revenue equal to taxes, since earnings are taxable. The state can establish a tax system, that the taxpayer should be differentiated and promote low income and Equity of high income taxpayer by using different methods of tax.

In this regard, the state faces a significant problem. It is quite difficult to establish such a tax system, which will help as a function of tax functions, As well as its social aspects of justice. Hus, Legislation is a task based on the economically grounded proposal Taxation of a tax

regime, which will not slow down the payer's economic activity and at the same time the appropriate level of tax payments in the budget.

The margin of tax deductions is a taxable condition. Which is optimal as a taxpayer, as well as for the state treasury. Move the conditional point on either side, creates contradictory circumstances, which is revealed chronic budget deficit or in political conflicts, in the disobedience of taxpayers to tax authorities, massive tax avoidance and Migration of the population.

1.2 Taxation methods and ability to use them

Optimal merger of direct and indirect taxes are required to create a flexible, fair and comprehensive tax system, but in our case direct taxes and, in particular, income tax effective, fair and social support mechanisms can be achieved Progressive tax taxation scaling and action. Since social support can be realized by taxation in a variety of ways and implies a progressive rate of income tax (As well as other tools: undeclared minimum, deduction System, benefits and other means of use) by establishing equalizing the income of different social groups of the population, reduction of social differentiation, which is closely linked to the principle of equality and fairness.

The use of any taxation depends on the economic condition of the country, main directions of the tax system, functions and goals. Separate any of them or give preference not right.

If you do not take into account the situation in the country. The state must define and choose the optimal option itself, because taxes play an important role in the socio-economic development of the country.

It is possible to use a regressive tax method to generate positive results in one country and significantly facilitate the improvement of the country's tax system and improve social conditions, but the use of this method in other countries is a completely different and negative result. Therefore, when choosing a method, the state of the economy should be considered, peculiarities of tax system and problems related to the equality of distribution of the income of the population, because the tax burden, which should be rationally distributed to the population and it's also convenient to remove.

It should be noted there is no clear causal connection on the one hand, inequality and between progressive taxes, and on the other hand poverty and between progressive taxes. However, we can say that the country where there is a progressive tax on poverty and inequality is low.

However, low and high economic growth may be in countries where there is a progressive tax and in countries where there is a so-called fixed income tax.

2. Implementation of progressive tax methods in Georgia

2.1 The peculiarities of the tax system of Georgia

After Georgia became an independent state, maximally trying to improve all economic indicators, however, none of the Georgian government has been able to do so to implement social-economic policy, which ensured the inclusive development of the country, to reduce unemployment, the problem of inequality in income and poverty.

Today, the income tax is uniform and the proportional method of taxation is used. It's rate is 20%². The proportional rate indicates taxation of the social direction. In this case, the tax pressure is more likely to cost the population less revenue. As a result the social differentiation of the society is strengthened.

Since the state should pay tax and money to pay higher taxes, and low-income (especially subsistence minimum) should help, do not overload it. Therefore, it is advisable and correct to some extent that the system of progressive rates will be restored and introduced again, but rates must necessarily be analyzed and more desirable is based on scientific research.

2.2. Progressive tax models.

Most OECD countries employ different types of progressive income tax structures, in which tax rates grow with increasing income (Olsen, J., Kogler, C., Stark, J., & Kirchler, E. 2017). Most of the overseas countries: Belgium, Sweden, Finland, Denmark, Spain, the United Kingdom, etc.³ Has a progressive income tax, but we will discuss, Spanish and Danish tax models. It should be noted that in Denmark as well as in Spain progressive tax is very different.

² Tax Code of Georgia Chapter XI "Income Tax" 2010 year.

³ Forbes. <http://forbes.ge/news/3234/romel-qveynebSia-dabali-gadasaxadebi>

Spain's progressive tax rate exceeds the average European rate. In Denmark, compared to Spain, the progressive income tax is higher⁴.

Table 1: Progressive income taxes in Denmark

From(euros)	Up to (euros)	Tax Rates
€ 0	€ 12.450	20%
€ 12.450	€ 20.200	25%
€ 20.200	€ 35.200	31%
€ 35.200	€ 60.200	39%
€ 60.000 \$ above	€	47%

Source: european.ge

Table 2: Progressive income taxes in Spain

Tax	Tax Base (in DKK)
0%	Up to 41 000
37.46%	41 001 – 279 800
43.48%	279 801 – 335 800
59%	335 8001 and over

Source: european.ge

As for the Gini coefficient, inequality in Denmark is 0.37. However, since taxes and transfer factors have been taken into account, this figure lasts up to 0.24. Therefore, taking into consideration these factors, it turns out that inequality decreases by 35%⁵. The same indicator in Spain is 0.34 in 2016⁶. Even though in both states, progressive taxes are high, such well-being indicators such as: Unemployment, inequality, poverty is still low. We will discuss some of the following factors:

⁴ Eurostat. <http://appsso.eurostat.ec.europa.eu/nui/show.do>

⁵ Social state and social democracy. 2014 year.

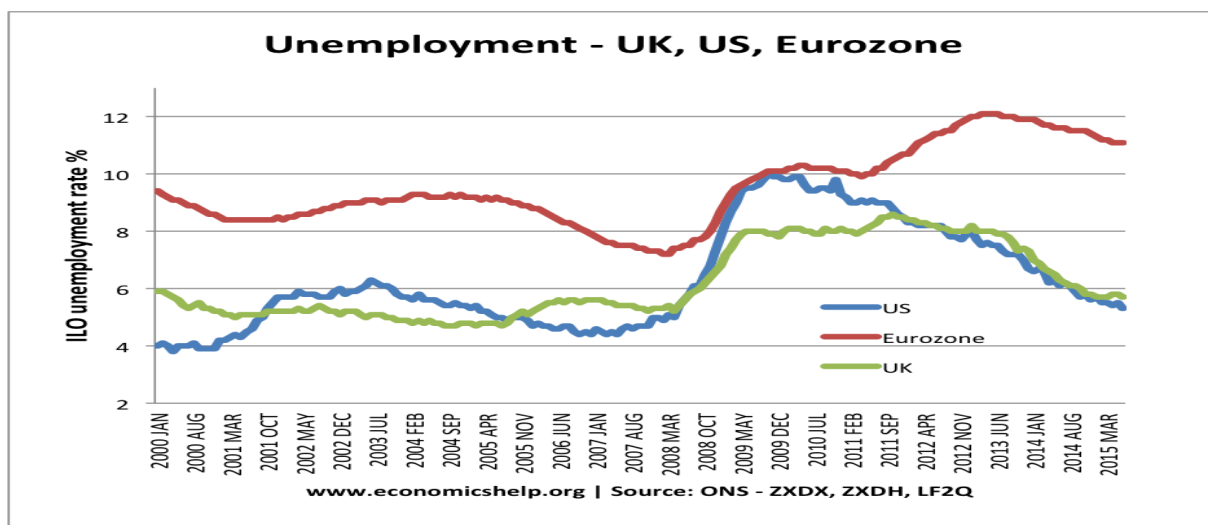
⁶ Eurostat. <http://appsso.eurostat.ec.europa.eu/nui/show.do>

First of all, it should be said that there is a high correlation between the progressive taxes and the degree of redistribution, however, the direct cause is not confirmed.⁷ So does not necessarily result in high quality distribution. Low level of redistribution indicates the existence of problems in certain areas, for example, economics and education.

Different studies show, that Spain has significant problems especially in the third level of education. Despite the fact that in Spain this indicator has increased and exceeds EU average indicators, In addition, the school's early abandonment rate and the number of people with poor education is quite high.

In Spain, there are two major factors influencing inequality and poverty. First, this is the catastrophic growth of unemployment since 2008 and the second is the size of the informal sector. Part of the researchers believe, that high level of unemployment creates significant problems in reducing re-distribution and inequality⁸.

Figure 1: Unemployment UK, US and EU.



Source: Forbises.ge

⁷ What nation has the most progressive tax system? <http://gregmankiw.blogspot.com/2011/03/what-nation-has-mostprogressive-tax.html>

⁸ WHY IS INCOME INEQUALITY SO HIGH IN SPAIN? Gradín., C, 2015, http://www.ecineq.org/ecineq_lux15/FILESx2015/CR2/p124.pdf

Denmark is undoubtedly an example of the development of the state of its development or prosperity. In Denmark, unemployment, poverty, inequality and social deprivation⁹ are not only the EU but also worldwide.

According to the Information Global Index (IDFI) of 2018, 10 countries around the world, which are the highest in different countries, including Denmark.

Table 3: Global Index of Information.

Country	Place	Score from 100,
Switzerland	1	68,4
Netherlands Kingdom	2	63,32
Sweden	3	63,08
Great Britain	4	60,13
Singapore	5	59,83
USA	6	59,81
Finland	7	59,63
Denmark	8	58,39
Germany	9	58,03
Ireland	10	57,19

Source: Institute for Development of Freedom of Information

Thus, Georgia can take some sort of a Danish state model of the welfare state in terms of implementing progressive taxes, as it provides the inclusive education of the society, more equality, less unemployment and poverty. However, we should also take into consideration that Georgia has a large non-informal sector like Spain, high unemployment rate and problems with management system. We should take into account, that progressive taxes will certainly not bring fair and inclusive development of the country, but with his introduction it will be another step forward to the country's socio-economic development.

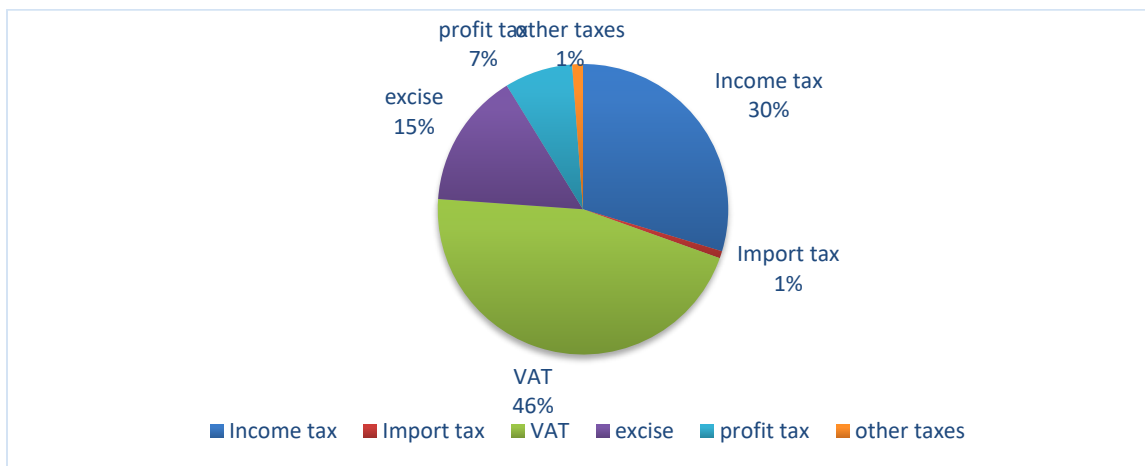
⁹Eurostat, http://ec.europa.eu/eurostat/statisticsexplained/index.php/File:Unemployment_rates_seasonally_adjusted_December_2015.png

2.3. Positive and negative sides of progressive taxes.

Progressive tax helps us to accomplish three goals of tax policy: Balancing inequalities between social groups, increasing budgetary revenue and to encourage entrepreneurial activities.

Of course the primary task of the progressive tax system is to solve the first issue, elimination of tax imbalances. For this purpose, we have to determine what kind of revenue is presented in comparison with the budget. Georgia's 2018 budget most of the tax revenues come in two taxes: VAT and income tax. (45.7% and 29.7%).

Figure 2: The Structure of Georgian Tax Revenue.



Source: Ministry of Finance of Georgia

Accordingly, it's easy to explain, most of the tax cargo comes to the final customer, because they are VG and income taxpayers, while only 7.6% of tax revenue on banking business and large business. Progressive taxes can therefore be divided into several categories and everything will be given its individual interest index.

Description of Income Tax Intervals:

At present there is a single rate for income tax in Georgia, regardless of the size of the income. It does not matter whether the salary will be 500 GEL or 5 000, all are taxed at 20%.

Thus, we may introduce a percentage scale and interest rates according to revenue, however, consider the average salary in Georgia according to the different sectors employed.

Table 3: The average monthly salary for different sector employees in Georgia (GEL)

Sectors	average salary
Financial activity	1500
construction	1413
State Governance	1313
Mining industry	1229
Transparency and communication	1219
Electricity, gas and water production and distribution	1126
Real estate with real estate	1095
Health and social security	843
The degrading industry	825
Trade	791
Hotels and restaurants	614
Agriculture	593
Education	470

Source: Statistical Office of Georgia

As a result, the average monthly salary starts from about 500 GEL and it increases according to the relevant sector.¹⁰ As a result of our analysis, we developed the following progressive taxation method:

- 0% - 500 GEL
- 10% - from 500 to 1000 GEL
- 20% - from 1000 to 1500 GEL
- 35% - 1500 to 3000 GEL
- 45% - 3000 GEL above

Positive features of progressive taxes:

- Additional budget sources of income are created at the expense of high income individuals, which is not provided in the normal system and most of the taxes come in

¹⁰ National Statistics Office of Georgia.

low and middle layers. Of course, it should not be so high that the tax is obliged to leave the country.

- Based on the fact that the tax burden increases with great revenue, it is automatically minimized to persons with small and medium income, which increases their competitiveness.
- Tax rate reduction will be equal to the increase in salaries for small and medium income persons, therefore, the state will facilitate business development.
- Progressive tax will facilitate the strengthening of middle class and its further development.
- Reduces the inequality between the income of the population.

As for the negative sides of the progressive taxation method. There is a misunderstanding, that the progressive taxation method prevents economic growth and stimulates the high income people. We do not agree with this assumption, because the world's developed and developing countries show the practice¹¹, that the progressive tax system is essential for the formation of social justice and economic welfare state, however, of course it is necessary to develop a tax model and then implement it according to the economic and other social conditions of the country.

Conclusion

So that, the real and perfect tax system in Georgia can not function properly without proper use of tax base and tax regulatory function. Tax policy should be derived from a specific situation and perspective strategic objectives.

Nowadays Georgia is actively developing different types of fiscal incentives, who may respond to failures of economic development of the country. In this context, it is of utmost importance to analyze European experience in terms of different fiscal approaches, while progressive tax is to be implemented in Georgia step by step, accompanied by relevant management reforms and industrial policies (Change of economy structure).

¹¹ Forbes.ge. Which countries have the lowest taxes.

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